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Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

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**JAN 14 1994**

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

In the Matter of  
Policies and Rules  
Concerning Toll Fraud

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CC Docket No. 93-292

AT&T'S COMMENTS

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## TABLE OF CONTENTS

	<u>Page</u>
SUMMARY .....	i
I. THE COMMISSION SHOULD REQUIRE CUSTOMER EDUCATION ON WAYS TO DETECT AND REDUCE TOLL FRAUD. ....	3
II. INDUSTRY EFFORTS TO REDUCE PBX FRAUD HAVE BEEN REMARKABLY SUCCESSFUL AND SHOULD BE SUPPORTED. ....	8
III. THE COMMISSION SHOULD DEVELOP RULES GOVERNING LIABILITY FOR PAYPHONE FRAUD BASED UPON THE PARTIES' RESPECTIVE ABILITIES TO CONTROL SUCH FRAUD .....	18
A. PPOs Should Be Initially Liable to IXCs for All Direct-Dialed Calls Placed from Their Telephones and Obtain Recourse When Appropriate from LECs .....	20
B. PPOs Who Comply with Reasonable Fraud Protection Requirements Should Be Relieved of Liability for Fraudulent Operator Services Calls .....	24
1. Domestic Calls .....	24
2. International Calls .....	26
C. Limitations of Liability in LEC Tariffs Should Not Prevent an Equitable Sharing of the Financial Responsibilities for Toll Fraud .....	28
IV. CELLULAR CARRIERS SHOULD BE RESPONSIBLE FOR IXC FRAUD CAUSED BY CLONING. ....	29

V.	CARRIERS WHO ATTEMPT TO QUERY LIDB ON A CALL CHARGED TO A LEC JOINT USE CARD, AND WHO OFFER TO PROVIDE CALL DETAIL INFORMATION ABOUT SUCH CALL, SHOULD BE REIMBURSED BY THE LEC FOR ANY RESULTING FRAUD LOSSES .....	31
VI.	THE COMMISSION SHOULD TAKE ADDITIONAL STEPS TO COORDINATE EXISTING INDUSTRY EFFORTS TO REDUCE TOLL FRAUD. ....	35
A.	The Commission Should Increase Its Participation in Existing Industry Toll Fraud Prevention Groups .....	35
B.	The Commission Should Encourage the Enforcement of Existing Criminal Statutes and the Adoption of More Effective Toll Fraud Prevention Statutes .....	37
CONCLUSION.....		39

#### APPENDIX A

Examples of AT&T Customer Education Materials  
On Toll Fraud

#### APPENDIX B

Optional AT&T NetPROTECT(sm) Offerings

#### APPENDIX C

Requirements for PPOS Seeking to Avoid  
Liability for Operator Services Calls

### SUMMARY

As the Commission recognizes, toll fraud is a serious problem that can affect the entire communications industry and all of its customers (NPRM ¶ 3). AT&T has previously urged the Commission to initiate an inquiry which encompasses the prevention of all types of toll fraud as well as the apportionment of toll fraud liability. AT&T thus welcomes the comprehensive approach to this problem evidenced in the NPRM. In particular, AT&T supports the Commission's involvement in the detection, prosecution and prevention of all types of toll fraud, as well as its efforts to establish principles that will assign equitably the responsibility for toll fraud when it occurs.

All carriers, suppliers and customers are co-dependent in maintaining the security of the public switched network. Therefore, AT&T supports the adoption of principles that assign liability for toll fraud in accordance with the respective ability of each party to control fraud and rules that encourage parties to implement fraud protection measures reasonably within their control. Thus, if toll fraud occurs as a result of a customer's or a carrier's failure to use reasonable and available security measures, the customer or carrier should bear the financial losses which result. In assessing the responsibilities of carriers, it is also important to assure that all involved carriers -- IXC's, PPO's, cellular carriers and LEC's -- bear their proportionate share of responsibility. As a result,

it may be necessary to impose rules that alter some of the current limitation of liability provisions in LEC tariffs for services designed to prevent fraud.

AT&T's experience validates the Commission's view that customer information and education is one of the most important tools in controlling such fraud. Thus, AT&T suggests below a number of educational messages which will help to reduce toll fraud, including proposed "warnings" on certain telecommunications equipment. Although tariff modifications alone are not likely to be as effective as other customer education programs, AT&T does not oppose a prospective requirement that carriers' tariffs also provide customers with warnings about the possible risks of toll fraud.

The general principles described above can be effectively applied to each of the specific types of fraud referenced in the NPRM. In some cases, particularly PBX fraud, significant economic incentives are already in place, and the interested parties have already forged processes that have significantly reduced the levels of toll fraud and reached equitable results in disputes over fraud losses. Likewise, in cases such as cellular "tumbling", cellular carriers have significant financial incentives and are working hard to develop technical solutions that would reduce toll fraud. In other areas, more work needs to be done and additional support and incentives from the Commission would be helpful. In all cases, however, it is

essential that the Commission fulfill its promise (NPRM ¶ 5) to "work with consumers and the industry to find solutions to each fraud problem without hindering the development or use of . . . new technologies."

In this regard, AT&T believes that the Commission can best help to prevent future toll fraud by joining in efforts to urge Congress and state legislators to adopt clearer and more specific criminal statutes regarding such fraud. In addition, the Commission should stress to law enforcement officials the need for increased enforcement of existing criminal statutes. These efforts could have a substantial impact in reducing the financial burdens of fraud, which are ultimately borne by the consuming public.

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AT&T'S COMMENTS

Pursuant to the Commission's Notice of Proposed Rulemaking ("NPRM") released December 2, 1993, American Telephone and Telegraph Company ("AT&T") submits the following comments on issues relating to toll fraud.

In Section I below, AT&T recognizes the importance of customer education in the fight against toll fraud and supports the Commission's customer education proposals. In particular, AT&T proposes several different notices that can be provided to customers to help them become aware of the risks of toll fraud and ways they can help to prevent it.

Section II describes the industry's success in reducing PBX fraud and assigning liability when there are legitimate disputes. AT&T shows that customer education, combined with network monitoring activities and a fair process for determining the financial responsibilities have effectively reduced the levels of PBX fraud, and AT&T seeks the Commission's support in continuing such efforts.

Section III below addresses the issue of payphone fraud and recommends a number of guidelines that will encourage PPOs, LECs and IXC's to take appropriate actions to control such fraud and to apportion equitably the responsibility for such fraud when it occurs. Section III also advocates changes in LEC tariffs to modify limitations of liability relating to LEC provision of blocking and screening services that are vital to the prevention of payphone fraud.

In Section IV, AT&T concurs with the Commission that cellular carriers have adequate incentives to control fraud caused by "tumbling." With respect to "cloning" fraud, AT&T supports the Commission's current proposals to implement technical requirements that would reduce the likelihood of future cloning losses. AT&T also proposes that the costs of cloning fraud should be borne by cellular carriers, rather than by IXC's and their customers.

Section V proposes that carriers who attempt to query a LIDB with respect to a LEC calling card call, and who offer call detail information on such call to the LEC, should be indemnified by the LEC against any fraud losses that may result, and AT&T further argues that limitations of liability in LEC tariffs should not shield them from responsibility in such cases. Section VI suggests other ways in which the Commission could act to coordinate existing fraud prevention activities and promote law



enforcement to reduce the costs of fraud for the industry and its customers.

I. THE COMMISSION SHOULD REQUIRE CUSTOMER EDUCATION ON WAYS TO DETECT AND REDUCE TOLL FRAUD.

In many cases, individual customers are in the best position to detect and prevent toll fraud, and in most cases customers, either individually or in the aggregate, bear the costs of toll fraud. As a result, the NPRM correctly proposes to require a number of education initiatives to inform customers about toll fraud risks and remedies.<sup>1</sup>

AT&T itself has developed many customer information packages and conducted many customer programs regarding toll fraud. AT&T estimates that in the past three years it has conducted fraud prevention programs for over 25,000 business customers. In addition, AT&T has published and distributed numerous brochures that provide customers with information on how to detect and prevent toll fraud.<sup>2</sup> As described below, such programs, if effectively designed and implemented, can sensitize customers to the possibilities of toll fraud, make them more aware of ways to

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<sup>1</sup> See, e.g., NPRM ¶¶ 13, 24, 40.

<sup>2</sup> Examples of such brochures are attached as Appendix A.

detect and prevent such fraud, and thereby lead to a reduction in fraud losses.<sup>3</sup>

AT&T therefore recommends that the Commission establish a requirement that all carriers collectively distribute an annual notice (such as a stand-alone bill insert) to all customers regarding toll fraud. For convenience, the notice could be delivered by the LECs.<sup>4</sup> The notice, which should also be provided to all new subscribers upon installation of service, would be general in nature and direct customers to their carriers or equipment suppliers for more detailed information. The text of the Notice could read as follows:

"NOTICE: The use of certain telecommunications equipment, particularly cellular telephones and Private Branch Exchanges (PBXs) and adjunct equipment, can bring with it the risk of theft of service, or "toll fraud". There are many steps you as a consumer can take, and a wide range of products and services you can order, which can help to prevent unauthorized use of your service and unanticipated charges to your account. For more information, contact your equipment vendor or manufacturer, your long distance carrier or your local telephone company business office at XXX-XXXX."

Such information will provide an effective and inexpensive way of notifying customers of the possibilities of toll

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<sup>3</sup> This effort has had substantial success in the area of PBX fraud. See Section II below.

<sup>4</sup> The expense associated with a LEC-distributed notice should be minimal, and could be shared by LECs and IXC's on a reasonable basis.

fraud and the availability of detailed information on fraud prevention measures.<sup>5</sup>

AT&T does not believe that the addition of fraud-related language in carriers' tariffs will be as effective as the customer notification program described above, or that the absence of fraud-specific language in a tariff is an unreasonable practice (see NPRM ¶ 24). Indeed, the Commission has already found that existing tariffs (which do not contain such language) provide customers with unambiguous notice that they may be responsible for fraudulent calls.<sup>6</sup> Nevertheless, AT&T does not oppose a prospective requirement that carriers include language in their tariffs alerting customers to the risk of toll fraud and their liabilities for fraudulent calls. If the Commission should require such tariff revisions, however, the specific language should be prescribed by the Commission, in order to prevent the needless exercise of

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<sup>5</sup> To the extent that the Commission believes it may be advisable to require specific warnings to cellular customers, AT&T recommends that the information should be provided by cellular carriers in connection with the cellular service application or as a cellular service bill insert.

<sup>6</sup> Chartways Technologies, Inc. v. AT&T Communications, Memorandum Opinion and Order, FCC 93-394 (released August 19, 1993), ¶¶ 11-13.

resolving future claims that the language is unclear or ambiguous.

The Commission could also facilitate the distribution of customer information by serving as a repository for fraud prevention materials created by members of the industry. This would enable the Commission, upon request, to provide customers with expanded amounts of information about toll fraud matters. AT&T would agree to make copies of the materials in Appendix A and similar information packages available to the Commission for such purposes.

AT&T also concurs with the Commission's proposal (NPRM ¶ 40) to amend Part 68 of the Commission's Rules to require that manufacturers of PBX-type equipment provide prominent and conspicuous warnings regarding the potential risk of toll fraud associated with use of their equipment. In order to provide all interested parties with clear guidance, and to avoid the possibility of future disputes over compliance with this requirement, AT&T recommends that the Commission adopt specific guidelines in connection with such warnings. AT&T recommends the guidelines should be as follows:

- (1) The warning should only be required for multi-line equipment capable of connecting incoming lines to outgoing lines. A requirement that a warning be provided for all CPE would be unnecessarily expensive and could dilute the impact of the warnings that are given.

(2) The warning requirement should be prospective only, because manufacturers often are unable to identify owners of previously manufactured equipment, especially equipment sold through unaffiliated dealers or in the secondary market.

(3) The warning should be contained in its own separate paragraph of the appropriate product documentation.

(4) The font size of the warning should be at least as large as the font size of the rest of the text on the page where the warning appears.

(5) The warning should be printed in bold or italicized type.

(6) For written documentation, the warning should be set forth on the title page of the document; for electronic documentation, the menu for the documentation should include a menu item entitled "toll fraud warning", and if this item is selected from the menu the warning should appear on the screen.

AT&T recommends that the warning for business-related CPE such as PBXs should be required only on standard installation, instruction and system administration manuals shipped or delivered with the product. It should not, as suggested in the NPRM (§ 40) be required on "all other literature accompanying the equipment," because such literature is typically not directed at the individuals who must read and act upon the warning, i.e., the system administrator, the installer and the end-user operator. In

addition, the warning should not be required on the exterior packaging, because such packaging is often removed before the equipment is delivered to the individuals who are in a position to act on the warning.

AT&T recommends that the text of the warning on PBXs and similar devices should read as follows:

"WARNING: POTENTIAL RISK OF TOLL FRAUD

Toll fraud, the unauthorized use of your telecommunications system by an unauthorized party (e.g., persons other than your company's employees, agents, subcontractors or persons working on your company's behalf) can result in substantial additional charges for your telecommunications services. You are responsible for the security of your system. There may be a risk of toll fraud associated with your telecommunications system. You are responsible for programming and configuring your equipment to prevent unauthorized use. Your system administrator should read all installation, instruction and system administration documents provided with this product to fully understand the features that can introduce the risk of toll fraud and the steps that can be taken to reduce that risk."

Adoption of these rules should provide PBX users with effective notice and sensitize them to the toll fraud risks associated with such equipment.

II. INDUSTRY EFFORTS TO REDUCE PBX FRAUD HAVE BEEN REMARKABLY SUCCESSFUL AND SHOULD BE SUPPORTED.

Part B of the NPRM concerns PBX fraud and seeks comments on ways in which the Commission can assist in developing incentives to reduce such fraud. PBX fraud is one area in which the marketplace has already responded to customer needs for assistance in toll fraud prevention and

has been very successful in establishing equitable procedures to resolve toll fraud disputes. The establishment of such principles, which was driven by the needs of customers, carriers, and equipment manufacturers and suppliers, has reinforced appropriate economic incentives for all parties involved. This, in turn, has led to greater vigilance and a significant reduction in the amount of PBX-related fraud losses.

The results of these efforts, combined with the education and monitoring activities discussed below, have been remarkable. The average loss due to CPE-based fraud has declined by over 75%, and the majority of cases reported today are 90% smaller than the average of two years ago. Moreover, the number of individual cases reported by customers has been cut in half.<sup>7</sup>

During the past three years, AT&T's customer education program has reached over 25,000 business customers with information about PBX-based fraud, and AT&T instituted its NetPROTECT(sm) offerings about two years ago. In addition, AT&T has implemented fraud detection capabilities

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<sup>7</sup> Non-cellular CPE-based fraud has also become much less important in comparative terms. AT&T estimates that the total of such CPE-based fraud losses reported to AT&T in 1993 is less than one-fifth of the fraud losses AT&T sustained during the same period on calls billed to LEC calling cards.

that have blocked thousands of known "hackers" from accessing its 800 network and other inbound applications. Over the same period, AT&T's network services and equipment entities have established a program designed to resolve fraud disputes that cannot be resolved by reference to AT&T's tariffs alone.<sup>8</sup> Under this voluntary negotiation process, liability is determined in each specific case, based upon a review of the applicable tariff and vendor contract requirements and each individual party's ability to control the equipment or network service element that enabled the fraud to occur. Over 98% of the disputes submitted to this process have resulted in settlements, and nearly 90% of the participants in the process gave it a favorable rating for "fairness."

In assessing the parties' respective liability for PBX fraud, it is clear that in most cases the customer is in the best position to identify toll fraud and to take steps to stop it.<sup>9</sup> Thus, the customer properly has the burden to

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<sup>8</sup> AT&T recognizes that the participation of its common carrier entity in this process is governed by its obligations under Title II of the Communications Act to collect its tariffed charges without unreasonable discrimination.

<sup>9</sup> The NPRM (§ 3) recognizes that customers have become more involved in toll fraud losses because "[c]ontrol over the use of telecommunications services has increasingly shifted from carriers to individual customers."



show that another party is responsible for any fraudulent calls placed through its PBX. Only the customer knows the complete package of CPE products, features and associated software it has purchased, and only the customer has direct access to such equipment. Moreover, the customer is the only party who can monitor all traffic passing through its PBX and authoritatively determine whether any specific call or calls are fraudulent. Thus, the customer alone is in a position to identify fraudulent calls and to re-program its equipment and associated software to shut down or modify the features that have permitted such calling to occur.<sup>10</sup>

IXCs can offer assistance to the customer through additional monitoring of traffic that transits their networks. However, fraudulent callers may use the services of many IXCs out of a single PBX. Thus, even though AT&T's NetPROTECT offering provides a sophisticated 24-hour-a-day traffic monitoring system for calls placed over AT&T's network, AT&T cannot monitor calls placed over other carriers' networks. Only the customer has access to all of its calling information through monitoring of its own PBX.

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<sup>10</sup> In AT&T's experience, occurrences of fraud have never required a customer to completely discard its existing CPE. In nearly all cases, the fraud can be controlled by making relatively simple changes in the existing equipment -- or simply by acting more prudently in assigning and monitoring the use of access codes.

AT&T and other carriers who offer network monitoring services constantly strive to improve their monitoring programs to stay ahead of fraud perpetrators, but IXC monitoring can only identify calling activity that is possibly suspicious. A spike in calling to a "high fraud" international location may be fraud, but it may also be the result of the customer's legitimate business activities in a new location. Only the customer can tell the difference.

The fact that IXCs have a limited ability to detect actual PBX fraud does not, however, mean that they lack incentives to control such fraud. To the contrary, competition drives carriers to anticipate and be responsive to customer needs. Moreover, IXC attempts to collect charges for fraudulent calls, especially when customers do not agree that they should be responsible, can have a devastating impact upon carrier-customer relations. Carriers may thus find themselves in a position of collecting toll fraud charges only to lose the customer's future business. Therefore, carriers have powerful incentives to cooperate with customers in creating an efficient dispute resolution process that will reach results based upon the parties' respective roles in allowing the fraud.<sup>11</sup>

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<sup>11</sup> Equipment manufacturers also have incentives to maintain good relationships with their customers. They cannot afford to reject all claims of liability without risking

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AT&T believes that the model described above -- which the vast majority of customers have found to be fair -- is the most appropriate way to resolve legitimate disputes concerning PBX fraud. This marketplace-driven process reinforces existing incentives for customers to understand the operation of their equipment and to monitor the calling activity they present to carriers. Rules that arbitrarily apportion liability without considering the parties' respective actions and relative ability to prevent fraudulent calling would skew those incentives with uncertain, and possibly arbitrary, results.

In AT&T's experience, the type of problems reported in the Pacific Mutual pleadings<sup>12</sup> have become rare, because of the aggressive educational campaigns and additional monitoring capabilities described above, as well as heightened customer awareness of fraud. As a result, the most important first step for the Commission is to institute the educational requirements described in Section I above.

In order to support customers' ability to protect themselves against PBX fraud, the Commission could also consider encouraging all IXCs to provide round-the-clock

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loss of future business, both from the customers directly involved and from others based upon the manufacturer's reputation for resolving fraud claims.

<sup>12</sup> See NPRM ¶¶ 16-19.

monitoring capabilities for customers who utilize PBX-like CPE, and to provide customers with prompt notification whenever suspicious calling patterns become apparent.<sup>13</sup> It is not clear, however, that these steps should be mandated, because market forces appear adequate to provide proper incentives. Indeed, because of customer interest and marketplace demands, AT&T already offers such services free of charge through its NetPROTECT(sm) Basic Service.<sup>14</sup> Through this service, AT&T monitors virtually all business calling over its network 24 hours a day, seven days a week, regardless of the CPE used by the customer. When suspicious calling patterns are identified, the customer is contacted, because only the customer can determine whether such calls

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<sup>13</sup> The monitoring process can work reasonably effectively when there is an existing relationship between the customer and the IXC. However, fraud from a single PBX can be the result of calling over many IXCs' networks. Thus, the ability to monitor and notify is significantly reduced when fraudulent calling occurs from a customer location that does not have an established relationship with the IXC whose network is being used.

<sup>14</sup> Other carriers have responded to customer needs with similar offerings. In addition, for customers who are willing to pay to obtain extra security, additional levels of NetPROTECT services are also available. See Appendix C for a description of these additional customer options. As competitive pressures and customer preferences increase, AT&T may be called upon to enhance its existing NetPROTECT offerings. AT&T will, of course, continue to respond to customer needs, regardless of any minimum regulatory requirements that may be established by the Commission.

are authorized and take focused action to protect themselves against fraud.<sup>15</sup>

After a customer has been contacted and confirms the existence of fraud, a carrier can provide various types of assistance to the customer to help stop the fraud. The specific assistance will depend upon the type of fraud, the nature of the customer's equipment, and the customer's preference. Such assistance may range from turning off the customer's service to providing advice on how the customer's CPE can be modified to prevent the fraud.

In addition, the Commission should consider establishing a mediation service which would be available on a voluntary basis to resolve disputes over liability for fraud. In any such mediation, the mediator should be guided by a determination of which party's actions enabled the fraud to occur, based upon a detailed review the facts of each particular case.<sup>16</sup> The inquiry should focus upon

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<sup>15</sup> AT&T opposes the suggestion (see NPRM ¶ 18) that the Commission establish requirements regarding the rates for monitoring services. AT&T also believes that the Commission should not require that specific calling patterns trigger customer notification procedures. Such matters should be left to the competitive marketplace as attributes of each carrier's service offering. Of course, through the tariffing process, the Commission can monitor the reasonableness of carriers' rates and practices relating to such services.

<sup>16</sup> The Commission's decision in Chartways implicitly recognizes these principles: "We noted that Chartways stipulated that it had 'the capability to restrict access

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the actual manner in which the fraud occurred and the actions of the party or parties who had control over the information, equipment or network element which allowed the fraud to occur. The review should also include issues such as the customer's failure to implement available fraud capabilities<sup>17</sup> and whether the customer received or was aware of the substance of mandatory warnings about toll fraud risks.<sup>18</sup> In all cases, the burden of proof should be upon the customer and damages should be measured by the tariffed rates for the fraudulently placed calls.

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to and egress from its PBX' at all times. Moreover, while the record contained no evidence that AT&T was negligent in any way with regard to the unauthorized calls, it also showed that Chartways had taken no steps available to it to detect or prevent unauthorized calling through its PBX" (NPRM ¶8).

<sup>17</sup> See NPRM ¶ 26.

<sup>18</sup> A carrier's or manufacturer's failure to provide specific mandatory warnings would not necessarily be a basis for assessing liability if the customer knew the substance of all such information without regard to its receipt of the actual warning. AT&T also agrees with the Commission's suggestion (NPRM ¶ 40) that if default codes on a PBX or similar equipment are set by a manufacturer, vendor or carrier, those codes should be fully explained to the customer. If the manufacturer sets such codes, the documentation accompanying the product should fully explain the function of the default codes and the risks associated with using the equipment without modifying such codes. If the default codes are set by another entity, it should be that entity's responsibility to provide a written explanation to the customer.

The Commission should not, however, adopt ARINC's suggestion that one of the objectives of new fraud rules should be "limited customer liability,"<sup>19</sup> regardless of whether the customer's actions were the actual cause of the fraud. Such a rule would create perverse incentives that would discourage customers from active involvement in fraud control. Moreover, it would inappropriately shift the economic burden for PBX fraud from customers whose systems have unnecessarily allowed such fraud to carriers, equipment suppliers and their customers.<sup>20</sup>

In sum, marketplace forces have led to the adoption of PBX fraud prevention and dispute resolution practices that create appropriate incentives for all concerned parties, and have also led to a significant reduction in such fraud. Accordingly, the Commission should rely upon and support the processes described above and implement similar standards in cases where it is directly called upon to resolve disputes over PBX fraud.<sup>21</sup>

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<sup>19</sup> See NPRM ¶ 17.

<sup>20</sup> Customers who voluntarily use PBX-type equipment that does not permit them to detect or control fraud should not be allowed to avoid responsibility for the fraud losses which result (see NPRM ¶19).

<sup>21</sup> In particular, the Commission should apply similar principles in cases involving fraudulent calls which were allowed to occur because of failures in LEC central office-based services that compete with PBX capabilities. As noted in Section III below, LECs presently have few

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III. THE COMMISSION SHOULD DEVELOP RULES GOVERNING LIABILITY FOR PAYPHONE FRAUD BASED UPON THE PARTIES' RESPECTIVE ABILITIES TO CONTROL SUCH FRAUD.

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In Part C of the NPRM, the Commission seeks comments regarding rules that should govern fraud involving private payphones. Specifically, the Commission inquires whether the Florida Public Service Commission's ("FPSC's") private payphone fraud rules should be adopted on a nationwide basis.

As described above, AT&T supports the development of principles that equitably assign liability in connection with all cases of toll fraud, including payphone fraud. Thus, AT&T recommends that the Commission adopt rules that require private payphone owners ("PPOs"), LECs and IXC's to participate in reasonable efforts to prevent fraud involving payphones, as well as rules that require such carriers to share fairly in fraud losses, based upon the extent to which their actions or omissions enabled those losses to occur. This is consistent with the Commission's view (NPRM ¶ 31) that "carriers should, as a general matter, be held accountable for the services they provide."<sup>22</sup>

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economic incentives to prevent fraud. Thus, additional rules or incentives may be necessary to reduce the costs of fraud that results from LEC service failures.

<sup>22</sup> Contrary to prior PPO arguments, however (see NPRM, ¶ 29), the relative financial wealth of parties involved in fraud losses should be irrelevant in determining

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Currently, IXCs and PPOs bear the principal responsibility for fraudulent interstate and international calling that involves the use of private payphones. The Commission has typically determined liability among these entities by determining whether the PPO was the IXC's "customer" under the applicable IXC tariffs. Such determinations have been based upon the actions the PPO took to prevent the possibility of fraud at its payphones.<sup>23</sup>

The LECs' role in payphone fraud prevention, and their financial responsibility in cases of actual fraud, have not yet been clearly defined by the Commission. LECs have had little incentive to assume such responsibility voluntarily, even when payphone fraud losses result from the failure of LEC blocking and screening services that were ordered by PPOs.<sup>24</sup> Indeed, LECs collect access charges from IXCs for every minute of every fraudulent interstate and international call from every payphone, even when the IXCs are held responsible or otherwise receive no revenues for those calls. Thus, LECs are actual (albeit unintended)

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responsibility. No carrier should be permitted to increase other carriers' fraud losses with impunity.

<sup>23</sup> See United Artists Payphone Corp. v. New York Telephone Co. and American Telephone and Telegraph Co., Memorandum Opinion and Order, FCC 93-387 (released August 18, 1993) ("United Artists").

<sup>24</sup> For example, the toll fraud in United Artists resulted directly from a failure in LEC blocking services.